IN THE UNITED STATES BANKRUPTCY COURT

FOR THE

SOUTHERN DISTRICT OF GEORGIA
Savannah Division

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| In the matter of: | |
| JAMES S. HOELTKE<br>VALERIE E. HOELTKE<br>(Chapter 7 Case 88-20667) | Adversary Proceeding<br>Number 89-2006 |
| Debtors | |
| JAMES CUTHBERT, SHEILA CUTHBERT, ROBERT GEHL, KAREN GEHL, and ROBERT DRAZEN | |
| Plaintiffs | |
| v. | |
| JAMES HOELTKE<br>VALERIE HOELTKE | |
| Defendants | |

**MEMORANDUM AND ORDER**

The above-captioned adversary proceeding was tried on October 20th and 25th. Plaintiffs seek a determination that certain

debts owed them by the Defendants are non-dischargeable under 11 U.S.C. Section 523 and alternatively seek a determination that the Debtors' discharge should be denied pursuant to 11 U.S.C. Section 727. Plaintiffs also seek the award of interest and attorney's fees. After consideration of the evidence introduced at trial, the briefs submitted by the parties, and a review of applicable authorities, I make the following Findings of Fact and Conclusions of Law.

## FINDINGS OF FACT

1) Jim and Valerie Hoeltke were engaged in the real estate business in the State of Florida for a number of years and held licenses to sell real estate issued by the State of Florida. Mr. Hoeltke obtained his real estate license in 1983 and it was revoked on October 18, 1988, by the Florida Real Estate Commission as the result of a finding that he had committed fraud, misrepresentation, concealment, false promises, false pretenses, dishonest dealing, and culpable negligence and breach of trust in a business transaction. Said final order was not contested by Mr. Hoeltke nor was it appealed (Exhibits 20 and 21). Debtors had advertised by newspaper and through printed flyers in the central

Florida area seeking to assist homeowners who were facing the threat of foreclosure (Exhibit 23). In connection with these activities they sometimes acted as agents for others and sometimes acted as principals on their own behalf.

2) In their dealings with all of the Plaintiffs herein, Mr. and Mrs. Hoeltke held themselves out as experienced investors and business persons, held themselves out as having special expertise in the real estate business, induced the Plaintiffs to repose a high degree of faith and trust in their handling of the business transactions that were entered into, and conceded that they felt bound by the legal and ethical standards applicable to real estate licensees in the State of Florida. Moreover, in all their dealings I find that Debtors were acting with a common purpose, in such a manner that each Debtor was the alter ego of the other and as such is individually responsible for the acts of the other.

3) In many respects the testimony of James Hoeltke contradicted that of the individual plaintiffs who testified. When there is conflicting evidence it is the Court's duty to judge the credibility of witnesses in reaching its findings of fact. In resolving this issue I have concluded that Mr. Hoeltke's credibility has been largely if not totally shattered by revelations made at

trial. I will not attempt to point out every inconsistency in his testimony or in the business records that he maintained but I observed that virtually throughout his testimony he was an evasive, argumentative and deceitful witness who admitted nothing when asked questions on direct examination and made admissions of facts which tended to hurt his case only when confronted with irrefutable documentary evidence.

With respect to discrepancies in his petition and schedules or in documents in his possession I will point out only a couple of illustrative examples from this lengthy record: (a) In question 2(d) of the statement of affairs in the Debtors' petition they revealed income in 1987 of approximately $30,000 when in fact their joint income for that year was approximately $69,800 (Exhibits 32, 33 and 34). Likewise, question 2(d) revealed joint income of approximately $15,000 for 1988, when in reality the Debtors had joint income of approximately $35,700 (Exhibits 35, 36 and 37). (b) The Debtors' statement of affairs fails to reveal their interest in any partnerships in which they might have engaged in business within the six years immediately preceding the filing of his case. In reality there were at least fifteen joint ventures they entered into within that period of time that should have been revealed (Exhibit 24). (c) Mr. Hoeltke failed to reveal his involvement in an

automobile sales business which activity was discovered by an examination of Exhibit 43. (d) In schedule B-2 of Debtors' petition, under question "P", they showed debts owing the debtor to be "none" when according to a financial statement given to various institutions they showed that they were owed some $93,000 in calendar year 1986. (e) A comparison of Exhibit 116 with Exhibit 41 shows than on checks numbered 368 and 369 totalling some $14,000 there was an alteration in which the memo line or the "For" line was erased after the check cleared the bank, apparently in an effort to conceal or to allow misrepresentation as to the true purpose for which those funds were initially tendered. (f) Debtor represented to a financial institution that his 1983 income was $71,495 (Exhibit 3) but filed his United States Individual Tax Return for that same year revealing to the government total income of $1,610.42 (Exhibit 4). Similarly, in 1982 he claimed income of over $35,000 when dealing with financial institutions but filed a return with the government revealing income of only $11,169 (compare Exhibits 1 and 2). Further, Debtors presented copies of a lease between themselves and Michael and Elizabeth Gabriel (relatives of Mrs. Hoeltke) in order to verify cash flow that they were allegedly receiving from rental income, in support of a mortgage application. Yet both Debtors acknowledge that Mr. and Mrs. Gabriel never rented any property from them, lived out-of-state and never signed a lease

(Exhibit 12). For the foregoing reasons, I conclude that the testimony of Plaintiffs on matters in which their testimony is in conflict is vastly more credible than the Debtors with respect to representations that were made during the time the parties were engaged in their business transactions.

4) The relief sought by the Plaintiffs, while similar if not identical in scope, arises out of distinct and separate transactions which will be separately addressed in this order.

## I. The Claim of Robert Drazen

5) Robert Drazen met the Hoeltkes through his brother and informed them that he was interested in purchasing a home because he was relocating in their area.

6) The Defendants showed their personal residence to Mr. Drazen who entered into a contract to purchase it for a total purchase price of $232,000.00. Drazen made a $5,000.00 earnest money deposit payable to Mr. Hoeltke (Exhibit 45). At the time of the negotiations Defendants represented to Mr. Drazen that it would be a waste of time for him to pay to have a title examination on the

property inasmuch as they were in the real estate business, were aware of the status of the title and could assure him that there were no liens other than those which were revealed on the contract for sale. Mr. Drazen delivered his $5,000.00 check to Defendants prior to the execution of the written contract.

7) Prior to that time, the Defendants' home had been the subject of a repossession action by Freedom Savings and Loan Association, holder of a second mortgage on their property, and a stipulation had been entered into between the Defendants and Freedom on March 13, 1987, under which Freedom agreed to cancel the judicial sale of their property in consideration of the Defendants' efforts to sell the property and payoff both first and second mortgages. Defendants stipulated that they were indebted to Freedom in the amount of nearly $59,000.00, and further agreed that Freedom was at liberty after a period of 110 days from the date of the stipulation to reschedule a judicial foreclosure if the property had not previously been sold. The Defendants also agreed to convey the property in lieu of foreclosure to Freedom anytime after 110 days had elapsed, within seven (7) days of a request by Freedom that they do so (Exhibit 44). At the time of the pending foreclosure by the holder of the second mortgage, the Defendants were also seriously in arrears in payments to City Federal Savings and Loan Association

which held the first mortgage on the property. Indeed, it appeared that no payment on the first mortgage had been made since July 1, 1986, a period of over one year prior to the negotiations with Mr. Drazen (Exhibit 49). None of this was revealed to Mr. Drazen at the time he delivered the $5,000.00 earnest money to Defendants. The parties agreed on a closing, even in the absence of a written contract, to be held on or before July 31, 1987.

8) Drazen learned approximately one week prior to July 31st that Defendants were not making any preparations to move although he was ready to proceed with the closing. After a series of excuses wherein Defendants continued to delay closing on the property, Mr. Drazen decided it was in his best interest to hire an attorney. After he did so, he was informed by the attorney that a number of liens were outstanding against the property. One of these was the second mortgage in favor of Freedom Savings and Loan Association which was in default and on which the 110 day grace period had expired. Upon discovery of this, he made demand on Defendants for return of his earnest money which was refused.

9) In addition, Drazen had paid the Defendants $4,000.00 to purchase certain furniture located in the residence which was to be left in place until the time of closing. In

preparation for moving into the home, Mr. Drazen and his wife-to-be made preparations to move from their separate homes which were outside the State of Florida, obtained Florida driver's licenses and bought additional furniture. When Mr. Drazen finally confronted Defendants about the missing money, he was informed that Defendants had spent the money. Defendants acknowledged an obligation to return the money to Mr. Drazen and in fact made a payment of $2,500.00 to him with respect to the purchase of the furniture. The balance of $1,500.00 was never paid (Exhibit 47). With respect to the $5,000.00 deposit, Defendant James Hoeltke executed a promissory note payable to Drazen in the amount of $5,000.00 dated September 2, 1987, bearing no interest. That note came due December 2, 1987, by its terms and has never been paid (Exhibit 48). The note also provided for attorney's fees in the event of default, if collected by an attorney.

## II. Robert and Karen Gehl

10) In response to one of the advertisements placed by Mr. Hoeltke previously referred to, he was contacted by Robert and Karen Gehl who were suffering some financial difficulties and were

behind in the mortgage payments on their personal residence. Defendants met with the Gehls on a number of occasions and determined that while the Gehls' house had been listed for some time at a higher price, the Gehls' main interest in any sale of their home was simply to salvage the money which they had invested in it, approximately $24,000.00. Mr. Hoeltke indicated to the Gehls that he believed he was in a position to pay them $24,000.00 for their equity in the property and take title to it thus freeing them up to reinvest in more moderate priced housing which they could better afford. He also offered to find them such an alternate home as part of an ongoing relationship.

11) Mr. Hoeltke advised Mr. Gehl that he wanted to have a title search done on the Gehls' residence in order to satisfy himself as to the status of title on the property. He returned within a day or so indicating that such an examination had been performed and that he was satisfied that sufficient value was in the property to justify paying Mr. Gehl what had been agreed on. Accordingly, a contract was entered into between the Gehls and Mr. Hoeltke for the purchase of the Gehls' residence located at 120 Coble Court, Longwood, Florida, for a price of $130,000.00. Said funds were to be applied to the approximate balance on the first mortgage of $77,500.00, on the second mortgage of $28,500.00,

leaving a payment of equity to the Gehls of $24,000.00 (Exhibit 58).

12) On June 2, 1983, Mr. Hoeltke induced Mr. and Mrs. Gehl to convey by quitclaim deed a one-half interest in their residence to Mr. Hoeltke "in order to protect his earnest money" (Exhibit 59). On July 17, 1983, Mr. Hoeltke procured a contract to sell the Gehls' home to John and Sandra Blanchard for a contract sales price of $132,900.00. The sale of the home was stipulated to be in "as is" condition (Exhibit 65).

13) Thereafter, Mrs. Hoeltke came to the Gehls' residence with blank real estate sales contract and asked to Gehls to execute it in blank, explaining that the Blanchard contract at a sales price of $132,900.00 had been lost and that Mr. Hoeltke needed a new one which he would fill in with the same figures as the original contract and get the Blanchards to sign it. In reliance on Mrs. Hoeltke's representations, Mr. and Mrs. Gehl executed the contract in blank and delivered it to Mrs. Hoeltke for use in that manner. Thereafter, the contract was completed showing a contract purchase price of $149,900.00 between the Gehls and Mr. Hoeltke as sellers and Mr. and Mrs. Blanchard (Exhibit 62). The Gehls were

never aware until the time of closing of any purchase price other than $132,900.00.

14) This altered contract revealed that a $10,000.00 earnest money payment had been made by the Blanchards and was being "held in escrow by First American Title Company". It was acknowledged by Jim Hoeltke that neither that $10,000.00 escrow payment, or the $1,000.00 escrow revealed on the lower priced contract, were ever placed in an escrow account or held in trust (Exhibits 62 and 65). Indeed, Mr. Hoeltke testified that the $10,000.00 was never paid but instead was a credit given the Blanchards on a home that they had "traded in" on the Gehl home when they executed a contract to sell their residence to Mr. Hoeltke for $65,000.00 (Exhibit 63). However, Hoeltke's $65,000.00 purchase price represented only the assumption of the balance of the Blanchards' mortgage. Ultimately, Mr. Hoeltke found purchasers by the name of David and Melinda Daum who bought the Blanchard home from him for $82,000.00, resulting in a realization to him of $15,012.28 in proceeds above what he had paid the Blanchards (Exhibit 66). As a result of this transaction, the net effect was that Mr. Hoeltke pocketed the proceeds of the sale of the Blanchard home. Although he reflected a portion of that profit as the $10,000.00 escrow deposit on the Gehl home which at closing should

have gone to Mr. and Mrs. Gehl, in fact, that money was not paid to the Gehls.

15) Mr. Hoeltke initially denied backdating the $149,900.00 contract between the Gehls and the Blanchards, but after being confronted with his deposition testimony which had previously been taken, he admitted that that contract was backdated to July 16, 1983, the day prior to the true contract date of July 17th (compare Exhibits 62 and 65). He also admitted that although he had obtained an appraisal on the property of $145,000.00 (Exhibit 64), he ran advertisements for the sale of the Gehls' home representing that the property had been appraised at $169,900.00 (Exhibit 61).

16) Moreover, notwithstanding the fact that the Gehls' contract to sell their home to the Blanchards provided that the home was sold in as is condition, Mr. Hoeltke rendered an invoice claiming an entitlement to be reimbursed the sum of $4,096.49 for repairs done on the Gehls' home as well as on a home which they were attempting to purchase through Mr. Hoeltke to replace the one they were selling (Exhibit 79). Although the Gehls authorized payment of that sum of money to Mr. Hoeltke out of the proceeds of closing (Exhibit 74), Hoeltke denied ever receiving that money after it became clear that the repairs to the Gehls' home should not have

been charged to them per the Blanchard contract, and the cost associated with the home the Gehls were purchasing should not have been charged to them since they were incurred by the previous owner. Despite Mr. Hoeltke's denial, he acknowledged having received $2,746.49 from the closing (Exhibit 75), and acknowledged receipt of "an additional deposit of $4,250.00 from the Blanchards (Exhibit 73). The total of those two sums equals the $6,996.49 improper reimbursement which he denied receiving, but clearly did receive.

17) While the closing between the Gehls and the Blanchards was pending, the Gehls needed a place to move and worked with Mr. Hoeltke to locate a home they were interested in. They succeeded in entering a contract with Jack and Marilyn Waldon to purchase their home for $87,000.00 which contract revealed a $10,000.00 earnest money deposit by the Gehls to be held by First American Title Company (Exhibit 81). Subsequently, a second contract was entered into at the same price between Mr. and Mrs. Waldon and the Hoeltkes (Exhibit 85). Ultimately, and apparently by use of the blank sales contract ruse, the Hoeltkes generated a contract with the Waldons whereby the house would be sold for $102,000.00 (Exhibit 86).

18) On October 17, 1983, Mr. and Mrs. Gehl showed up, on very short notice by Mr. Hoeltke, at the offices of First American Title Company to execute the closing documents for the sale of their home to the Blanchards. When they looked at the closing statement (Exhibit 68) and saw a purchase price of $149,900.00, they advised the closing agent that the closing price was wrong. They were informed by him that Mr. Hoeltke had provided him with the figures that went on the closing statement, and told them that if they did not sign the documents to close with the Blanchards, they would end up being sued by the Blanchards and Mr. Hoeltke. After all deductions were made on the closing statement, the Gehls should have received proceeds of $18,105.33. However, because of the invoice which Mr. Hoeltke had presented and the monies that were paid to him, the Gehls received only $10,108.84 (Exhibit 76). In reality, not only were the Gehls unaware that the contract sales price was $149,900.00, but Mr. and Mrs. Blanchard deny paying that much money and assert that the contract they closed on was for a sales price of $132,900.00 (Exhibit 80).

19) When Mr. Hoeltke was called upon to explain the discrepancies in this three way transaction, he referred to Exhibit 62 showing a $10,000.00 earnest money deposit, Exhibit 68 revealing a $17,150.00 earnest money deposit, and Exhibit 66 showing

$15,012.28 as proceeds to the Blanchards from the sale of their home. His only explanation was that, although the figures did not match, they all should be the same. From his testimony, I can only conclude that the transaction he intended to effect was to take the profit from the sale of the Blanchards' home and treat it as a credit to the Blanchards on their purchase of the Gehls' home. It is uncontradicted, however, that the monies were not paid to the escrow agent but instead were held by him. Thus it is clear that he profited at least $15,000.00 and possibly as much as $17,000.00 from crediting the Blanchards profit to the Gehls' transaction, without actually paying over those sums to the Gehls. This resulted in their realizing $15,000 - $17,000 less from the proceeds of their home than they were entitled to recover. Hoeltke admits that the dollar figures shown on Exhibit 68 were inflated and that the Blanchards were able to obtain 100% financing of the purchase price of their new home as a result of it. (See line 202 on the closing statement (Exhibit 68) which shows that the principal amount of the new loan was essentially the same amount as the true contract price of $132,900.00.) In addition to the $15,000.00 to $17,000.00 which Mr. Hoeltke profited from the Blanchard-Gehl transaction, he received either in cash at closing, or as a result of his acknowledgement (Exhibit 73), an additional $6,996.49 which he was not entitled to receive.

20) Mr. Gehl was advised by the closing agent to contact Mr. Hoeltke to reconcile the monetary aspects of the transaction that he disagreed with, and he ultimately was able to do so. Hoeltke not only was able to explain the shortages, but advised Gehl that he needed an additional $10,000.00 in earnest money to preserve the contract to purchase the home from the Waldons (Exhibits 81, 85 and 86). Gehl was desperate, having sold his other house, receiving far less than he believed he was entitled to, and was left with no option but to try and close the Waldon contract. Therefore, he agreed to pay $8,500.00 from the net of $10,000.00 he had received from the sale to Blanchard and Hoeltke agreed to credit him with the remaining $1,500.00 so that his $10,000.00 earnest deposit on the Waldon home would be considered paid in full. Apparently, the Waldons discovered the higher priced contract on their home prior to closing and, suspecting treachery, refused to close. As a result, all of the earnest money paid by the Gehls to the Waldons or the Hoeltkes was lost. The exact reasons for this turn of events are unclear from the record but plainly were not the fault of the Gehls. Rather, any fault for the Waldons' quite reasonable suspicion lies with the Hoeltkes.

21) While it is difficult to pinpoint the precise amount which the Defendants realized as a result of this transaction because of the fraudulent and unreliable nature of the contracts and closing statement previously outlined, it appears that they profited at least to the extent of $15,000.00 to $17,000.00 on the Blanchard-Gehl transaction, $6,996.49 as a result of the expenses they wrongfully obtained reimbursement for from the proceeds of the Gehl sale, and $8,500.00 which the Gehls delivered for earnest money toward the Waldon contract which was misappropriated and lost.

## III. James and Sheila Cuthbert

22) Sheila Cuthbert and Valerie Hoeltke have known each other since high school, and mutually described each other as having been best of friends and as close as sisters. They served as maid of honor in each other's wedding and maintained a close family relationship, even to the extent that one of them had served as godparent for a child of the other. Because of their relationship, the Hoeltkes offered to Sheila Cuthbert and her husband James Cuthbert the opportunity to invest in some of the real estate transactions they were engaged in. Initially those transactions

were handled in a manner that resulted in profits being earned by both the Cuthberts and the Hoeltkes.

23) After their initial success, on March 20, 1984, James Cuthbert entered into a joint venture agreement with James Hoeltke for the purchase of property located at 1509 Terrace Drive, Sanford, Florida (Exhibit 97). Cuthbert agreed to supply all the money necessary to purchase, recondition, advertise, and sell the property. Hoeltke agreed to provide expertise to the same, and it was provided that all net profits would be divided equally between the two of them. On March 20, 1984, James Hoeltke took title by warranty deed in his name to the same property by conveyance from William and Bessie Bradwell (Exhibit 99) for payment of $1,000 and assumption of their outstanding mortgage. On or about June 16, 1984, Hoeltke entered a sales contract to convey said property to Wayne and Rene Dykes. The Dykes contract price was $51,900.00 with a closing on or before August 31, 1984 (Exhibit 101). That contract committed Hoeltke to hold a second mortgage with a five year balloon note in the amount of $10,900.00. Hoeltke obtained $3,500.00 in earnest money deposits from Mr. and Mrs. Dykes. The contract with the Dykes expired without being closed, and Mr. and Mrs. Dykes leased the property for a period of time after the expiration of the contract. Thereafter, on or about July 25, 1985, Hoeltke entered

into a contract to sell the same property to Michael and Hellene Carson for $49,900.00, and obtained a $1,000.00 earnest money deposit. The closing statement dated August 2, 1985 (Exhibit 108), revealed that a total of $15,000.00 in deposit or earnest money was credited to Mr. and Mrs. Carson which Mr. Hoeltke took for his own use. Under the joint venture agreement, Mr. Cuthbert and Mr. Hoeltke were to split whatever profit remained after expenses on a fifty-fifty basis (See Exhibit 97).

24) Although he demanded an accounting for the expenditures and the income from the transaction on a number of occasions, Mr. Cuthbert's demands were ignored (Exhibits 111, 112 and 113). An examination of Exhibits 107 and 108, reveals Hoeltke received $16,000.00 in earnest money from the Dykes and/or Carsons.

25) After this litigation ensued, Cuthbert was able to obtain an accounting for the income and expenses that arose out of the transaction on Terrace Drive and discovered that total income including rent, utility refunds, and deposits and earnest money totaled $25,523.82. Hoeltke and Cuthbert had both paid expenses that had arisen with respect to that property but the vast majority of those expenses were paid by Hoeltke. The net expenses which he paid after deducting credit for what Cuthbert paid was $11,315.04.

This yields a profit on the entire transaction of $13,208.78, half of which was Mr. Cuthbert's, or a total of $6,604.39. Said profit was due on or about August 2, 1985, at the time of the closing with the Carsons. This money has never been repaid.

26) The final transaction involved both Sheila and Jim Cuthbert, and related initially to property located at 2517 Fox Squirrel Court. On February 22, 1984, a joint venture was entered into between James and Sheila Cuthbert, and James and Valerie Hoeltke to acquire, recondition and sell the subject property and to divide all the profits equally after expenses were paid (Exhibit 121). The joint venture further showed that a total of $80,000.00 was invested by the parties, with James Cuthbert supplying $50,000.00, and Hoeltke supplying $30,000.00. However, unbeknownst to James Cuthbert, his wife Sheila Cuthbert had advanced the $30,000.00 to Mr. Hoeltke for his share under a verbal agreement that she would in fact be a silent partner in the joint venture and would be entitled to the profits. On or about February 22, 1984, Hoeltke executed a contract to purchase the subject property from Raymond and Mary O'Toole for payment of $80,000.00 equity, together with an assumption of the outstanding indebtedness not to exceed $133,000.00 (Exhibit 122). On February 28, 1984, a closing occurred, and the Hoeltkes and Cuthberts took title to the subject

property in accordance with that sales contract (Exhibits 123 and 124). The Cuthberts were informed by Hoeltke that he had a purchaser for the property, and in fact the home was occupied at that time by an individual whom they believed to be the prospective purchaser. Although that person made a subsequent offer to Mr. Hoeltke to purchase the property, Mr. Hoeltke did not inform the Cuthberts of that offer but rather rejected it on his own. Ultimately, on or about April 24, 1984, the Hoeltkes and the Cuthberts entered into a contract to sell the subject property to Jan Clem for a stated consideration of $133,000 (Exhibit 125). However, the addendum made it clear in paragraph one that what was contemplated was a transfer of Ms. Clem's equity in two other properties, and the obligation to convey the property on Fox Squirrel Court was contingent on a simultaneous closing of these properties located at 590 Diane Circle and 1105 Landmark Towers Condominiums. In fact, on May 8, 1984, simultaneous closings took place at which time the Hoeltkes and Cuthberts acquired title to the Diane Circle and Landmark Towers properties (Exhibits 126, 133 and 155). Thereafter, appraisals were obtained on the two properties acquired by the joint venturers which revealed appraised value on Diane Circle at $55,000.00 and on Landmark Towers of $150,000.00 (Exhibits 134 and 156). The Diane Circle property was subject to a $14,000.00 mortgage, and the Landmark Towers condominium was debt

free at the time of the acquisition on May 8, 1984. On July 23 and 25, 1984, under the representation that he had purchasers ready to close on both properties, Hoeltke induced the Cuthberts to convey their interest in the properties to Mr. and Mrs. Hoeltke by quitclaim deed (Exhibits 140 and 159). Thereafter, on July 24, 1984, Hoeltke, armed with the appraisals he had obtained and with title to the properties by virtue of the quitclaim deed from the Cuthberts, mortgaged both properties without the knowledge or consent of the Cuthberts.

27) The mortgage transaction on Diane Circle involved a $54,000.00 new mortgage loan and, according to the closing statement, resulted in $38,013.57 cash being paid to the seller, Jan Clem. However, Hoeltke admits that these monies were in fact received by him since he was the owner of the property. Apparently unbeknownst to the mortgage company, the entire closing transaction between Clem and Hoeltke was fraudulently represented to have been entered into by the parties for the purpose of Ms. Clem acquiring the property when in fact the transfer had already occurred. Hoeltke admits that the $48,013.57, less the $13,266.73 which was shown as being due to the borrower, was received by him. It is unclear whether the $13,266.73 was paid to Jan Clem, the seller in fact, or whether that was the amount of money necessary to pay off

the first mortgage. With respect to the Landmark Towers condominium, the net amount paid to the borrowers allegedly to "refinance" a nonexistent loan on this property was $56,116.90. Not long thereafter, upon discovering that the Hoeltkes had mortgaged both properties without his knowledge and in contravention of his wishes or any agreement for them to do so, Jim Cuthbert demanded that he be repaid his investment in the property. On July 30, 1984, the Hoeltkes repaid a total of $54,141.46 which represented his initial investment of $50,000.00 plus expenses that he was reimbursed for. The Hoeltkes did not repay the $30,000.00 which had been invested by Mrs. Cuthbert. Since Mr. Cuthbert had no knowledge of his wife's investment, he made no further demand on them since he thought he had received his investment back in full.

28) Sheila Cuthbert learned that the property had been mortgaged because her husband reacted so angrily when he learned about it and she was also aware that he had been repaid his investment. Thereafter, operating with that knowledge, she visited Valerie Hoeltke and demanded repayment, but was refused. Valerie said that her $30,000.00 which was tied up in those two pieces of property would be reinvested for her. When the Hoeltkes were later unable to repay the $30,000.00 to Sheila Cuthbert, they offered to pay her 8% per annum on her investment because she pointed out that

her $30,000.00 which had allegedly been "reinvested" was not earning her any money. In fact, four checks for $200.00 each were delivered by the Hoeltkes to Mrs. Cuthbert, but she never received any repayment of principal for the investment she made. Neither Sheila nor Jim Cuthbert ever reacquired record title to either of the properties. The Landmark Towers property was ultimately foreclosed upon after the Hoeltkes were unable or unwilling to make the monthly mortgage payments that they were obligated to make as a result of the loan obtained without the Cuthberts' authorization. The Diane Circle property ultimately was sold to a third party and none of the profit, if any, realized from that sale by the Hoeltkes was returned to either Jim or Sheila Cuthbert. As a result of the Hoeltkes activities, Sheila Cuthbert's investment of $30,000.00 made in April of 1984 has never been repaid. The Hoeltkes have admitted receipt of over $90,000.00 in loan proceeds from the two closings, less the $54,000.00 paid as a return of investment to Jim Cuthbert, leaving them with a profit of at least $36,000.00 without having made any investment of their own funds.

## CONCLUSIONS OF LAW

Plaintiff seeks to have the debt owing to it excepted from discharge pursuant to 11 U.S.C. Section 523(a)(2)(A), which provides in relevant part:

> (a) a discharge . . . does not discharge an individual debtor from any debt--
>
> (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by--
>
> (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition.

"Because of the very nature and philosophy of the Bankruptcy law the exceptions to dischargeability are to be construed strictly, Gleason v. Thaw, 236 U.S. 558, 35 S.Ct. 287, 59 L.Ed. 717 (1915), and the burden is on the creditor to prove the exception. Danns v. Household Finance Corporation, 558 F.2d 114 (2nd Cir. 1977)." In re Hunter, 780 F.2d 1577, 1579 (11th Cir. 1986).

To prevail, the creditor must prove by clear and convincing evidence that:

> . . . the debtor made a false representation with the purpose and intention of deceiving the creditor; the creditor relied on such representation; his reliance was reasonably founded; and the creditor sustained a loss as a result of the representation.

Id. (false pretenses or false representations). See also Matter of Carpenter, 53 B.R. 724, 729 (Bankr. N.D.Ga. 1985) (actual fraud).

> The debtor must be guilty of positive fraud, or fraud in fact, involving moral turpitude or intentional wrong, and not implied fraud, or fraud in law, which may exist without the imputation of bad faith or immorality.

Hunter, at 1579. In an action for false pretenses or representation,

> [t]here must be actual overt false pretense or representation to come within the exception. The absence of explicit representations concerning financial conditions by the bankrupt requires a holding that there have been no false pretenses or false representations.

Hunter, supra at 1580, citing Davison-Paxon Co. v. Caldwell, 115 F.2d 189 (5th Cir. 1941), cert. denied, 313 U.S. 564 (1941).

"Therefore, a mere breach of contract by the debtor or a mere failure to fulfill a promise to pay for goods, is, without more, insufficient to establish nondischargeability . . . . By the same token, however, fraud can be established from circumstantial evidence." Chase Manhattan Bank, N.A. v. Flowers, CV587-036, 9-10 (S.D.Ga. Jan. 11, 1988) (citations omitted). However, actual "fraud is 'in itself subtle' and circumstances apparently trivial or almost inconclusive, if separately considered, may by their number and joint operation be sufficient to constitute conclusive proof." Grainger v. Jackson, 122 Ga. App. 123, 176 S.E.2d 279 (1970).

As applied to the facts in this case, I find that each Plaintiff has established the fraud elements of Section 523(a)(2)(A) by clear and convincing evidence.

As to Robert Drazen, Debtors falsely represented that there were no unrevealed liens on their home and represented that they would be able to perform under their contract. In fact, there were a number of undisclosed liens, they were in default on both their first and second mortgages, and their home was under immediate threat of foreclosure.

In reliance on their representations, Drazen paid $5,000 earnest money and purchased, yet never received, certain furniture

for $4,000. Debtors repaid only $2,500 of that sum and Drazen has been damaged in the amount of $6,500. I find his reliance on Debtors' representations to be reasonable given their expertise and the fact that they were licensed real estate agents in the State of Florida, held themselves out to be competent and trustworthy, and were aware that Drazen was relying on their professionalism throughout the transaction.

As to Mr. and Mrs. Gehl, Debtors engaged in an elaborate scheme of misrepresentation and deception, resulting in the Gehls' loss of the entire $24,000 equity they had in their home. Debtors converted earnest money deposits to their own use, falsified sales contracts, and double charged for expenses allegedly incurred. After pocketing earnest money due to the Gehls on the sale of their home, Debtors exacted an additional $8,500 to pay as earnest money on the home the Gehls intended to purchase, and converted that money as well. Debtors profited to the extent of at least $30,500 as a result of these multiple transactions; however, had they paid the Gehls the agreed upon equity of $24,000, Debtors would have been entitled to keep those profits for their efforts. Thus, I conclude that the damage recoverable by the Gehls is limited to $24,000.

As to Mr. Cuthbert, Debtors again converted earnest money deposits, rental income and other funds. As to both

Cuthberts, Debtors took $80,000 and purchased a home subject to a large mortgage for investment. Later they traded that home for two properties which were nearly debt free. However, by misrepresentations and fraud, Debtors induced the Cuthberts to convey title to those two properties to Debtors, who then mortgaged the property without the knowledge or consent of the Cuthberts.

Debtors pocketed the proceeds of the loans, eventually paid all Mr. Cuthbert's investment back, but never repaid the $30,000 investment of Mrs. Cuthbert. Ultimately, one property was lost through foreclosure and the other was sold without any further reimbursement to Mrs. Cuthbert on her investment.

The Cuthberts placed a high degree of faith and trust in the Debtors, not only because of the profession Debtors engaged in as realtors, but also because of a long-time close personal relationship. Debtors acknowledged that they were aware that the Cuthberts relied upon their expertise and I conclude that such reliance was reasonable. Mr. Cuthbert's damages amount to $6,604.39 and Mrs. Cuthbert's total $30,000.

Plaintiffs seek the recovery of interest and attorney's fees in addition to the principal debt. After careful consideration of the authorities cited, applicable statutes and legislative

history, and the arguments proffered by able counsel on both sides of this issue, I find that the award of interest is appropriate, but am compelled to deny the award of attorney's fees.

Congress never intended nor will this Court countenance the use of the bankruptcy system as a safe haven for the dishonest debtor. Bankruptcy relief was intended by Congress to provide the honest but unfortunate debtor with a fresh start in life, relieved from the distress and burden of excessive debt. Local Loan Co., v. Hunt, 292 U.S. 234, 244, 545 S.Ct. 695, 699, 78 L.Ed. 1230 (1934) (emphasis provided). Pursuant to that policy, Congress and the Courts have placed a heavy burden on creditors to prove the fraud exception to discharge by clear and convincing evidence. Hunter, 780 F.2d at 1579. Once a creditor meets this heavy burden of proving the debtor's malfeasance, the fresh start policy implemented for the benefit of the honest debtor is no longer applicable. Relief intended for the honest should not inure to the benefit of the dishonest and once dishonesty is clearly established, non-bankruptcy rules should apply. In re Hunter, 771 F.2d 1126 (8th Cir., 1985); In re Wilson, 12 B.R. 363 (M.D.Tenn. 1981).

In ascertaining the appropriate measure of damages in fraud actions, Courts have grappled with whether to measure damages based upon out-of-pocket expenditures of the plaintiff proximately

caused by the defendant's fraudulent conduct, or whether to base damages on the benefit-of-the-bargain which would have been realized by the defrauded plaintiff but for the defendant's malfeasance. Wilson, 12 B.R. at 366-67. The Wilson court adopted the benefit-of-the-bargain rule, reasoning that limiting relief to the defrauded creditor to out-of-pocket expenses would not discourage fraudulent conduct since the defrauding debtor would essentially have no risk. "[I]f he is not called to account, he enjoys his plunder; if he is called to account, he merely gives back what was not rightfully his, and thus is no worse for the fraud." Id. at 366 (quoting 37 Am. Jur. 2d Fraud and Deceit §356 (1968)). Thus, "policy considerations require that when a debt is excepted from the discharge under 11 U.S.C. Section 523(a)(2)(A), the creditor is entitled to recover compensatory damages proximately caused by the fraud measured by the benefit-of-the-bargain rule." Id. at 370. I find this rationale compelling, particularly in light of the egregiousness of the Debtor's conduct and will award damages based upon the benefit-of-the-bargain rule including interest as follows: Interest is allowed on the Drazen claim of $6,500.00 at 12% from July 31, 1987, through date of judgment. Interest is allowed on the Gehl claim of $24,000.00 at 12% from October 17, 1983, through date of judgment. Interest is allowed on the James Cuthbert claim of $6,604.39 at 12% from August 2, 1985, through date of judgment. Interest is allowed

on the Sheila Cuthbert claim of $30,000.00 at 12% from July 24, 1984, through date of judgment.

Additionally, Plaintiffs seek the recovery of attorney's fees incurred in the prosecution of this action. The Eleventh Circuit addressed the issue of attorney fee shifting in Section 523(a)(2)(A) actions in In re Fox, 725 F.2d 661 (11th Cir. 1984), setting forth the clear mandate that in the absence of specific statutory authority for such award, the shifting of a prevailing party's fees in a Section 523(a)(2)(A) action constitutes reversible error. After a diligent search, I have found no statutory authority nor has counsel cited any. In light of this binding precedent, I regretfully must deny Plaintiffs' attorney fee motion.

Plaintiffs alternatively assert a Section 727 objection to discharge. However, I am constrained from considering this issue as the objection was untimely filed. Bankruptcy Rule 4004(a) plainly requires that a complaint objecting to discharge shall be filed not later than sixty (60) days after the first date set for the meeting of creditors. Bankruptcy Rule 9006(b)(3) specifically removes any Court discretion for allowing late filing under Rule 4004, explicitly limiting enlargement to the precise terms of Rule 4004(b), which allows extension for cause only if sought within the sixty day statutory deadline. The Clerk's entry in the record shows

that the first meeting of creditors was scheduled for January 20, 1989. Plaintiffs' Section 727 objection was filed on April 27, 1989, ninety-seven (97) days after the first date set for the meeting of creditors. After reviewing the applicable case law, I find that Plaintiffs do not qualify under any of the few very limited exceptions to the strict application of Rule 4004.

Since I do not find that the Plaintiffs have satisfied the requirements of Rule 4004 nor qualify for the very limited exceptions to the application of that rule, I must dismiss the Plaintiffs' Section 727 objections as untimely filed.

## O R D E R

Pursuant to the foregoing Findings of Fact and Conclusions of Law, IT IS THE ORDER OF THIS COURT that Plaintiffs be awarded damages in the amount of $6,500.00 on the Drazen claim, plus interest at the rate of 12% per annum, calculated from July 31, 1987, through date of judgment; $24,000.00 on the Gehl claim, plus interest at the rate of 12% per annum, calculated from October 17, 1983, through date of judgment; $6,604.39 on the James Cuthbert claim, plus interest at the rate of 12% per annum from August 2, 1985, through the date of judgment; and $30,000.00 on the Sheila

Cuthbert claim, plus interest at the rate of 12% per annum from July 24, 1984, through date of judgment.

IT IS FURTHER ORDERED that the Plaintiffs' request for attorney's fees is denied.

IT IS FURTHER ORDERED that Plaintiffs' Section 727 objection to discharge is denied.

Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia
This 21st day of December, 1989.